GOVERNMENT OF INDIA
FINANCE
LOK SABHA

UNSTARRED QUESTION NO:4370
ANSWERED ON:11.08.2017
Local Currency Loan in Indian Rupees
Majhi Shri Balabhadra

Will the Minister of FINANCE be pleased to state:

(a) whether the Government has explored the possibility for availing of local currency loan in Indian Rupees instead of LIBOR based dollar denominated loan from World Bank and Asian Development Bank (ADB) which has inherent exchange rate fluctuation risk;

(b) if so, the details thereof; and

(c) the comparative advantage and disadvantage of local currency loan over dollar denominated LIBOR based loan?

Answer

MINISTER OF STATE IN THE MINISTRY OF FINANCE (SHRI ARJUN RAM MEGHWAL)
(a) Yes Sir.

(b) Loans from the International Bank for Reconstruction and Development (IBRD) of the World Bank are committed in United States Dollars (USD), and the implementing agency can access INR financing from IBRD by exercising the built-in currency conversion option in IBRD loans to convert disbursed and outstanding amounts into Indian Rupees (INR) at any time during the life of the loan. The Government of India regularly liaises with IBRD on the possibility of converting new and existing loans into INR.
The availability of INR financing, and the terms and conditions that IBRD could obtain, would depend on market conditions at the time of execution of the conversion. IBRD could source INR financing either via the swap market or by direct bond issuance.
The Government of India had also requested the Asian Development Bank (ADB) to explore the possibility of providing the option of local currency financing in addition to USD denominated loan option for the ADB assisted projects in India.
In response, ADB has proposed to introduce an option of local currency financing for the "Second West Bengal Development Finance Programme (WBDFP-II)", which comprises a loan amount of USD 300 million. The said loan has been negotiated between Government of India, ADB, and Government of West Bengal on 7th July, 2017. The proposal is yet to be considered by the Board of Directors of ADB.
The local currency financing option proposed by ADB for the above mentioned project provides Government of India an option to request disbursement of loan in Indian Rupee, either in part or fully, in addition to the prevailing option of seeking disbursement in USD. However, the local currency financing option will be at the discretion of Government of India.

(c) The comparative advantages and disadvantages in terms of local currency loan over dollar denominated LIBOR based loan depend on the needs and circumstances of the project and the borrower, and involves a tradeoff between cost and risk.
In general, borrowing in local currency would reduce the foreign exchange risk of a borrower who does not have a source of USD revenues. However, in shallow domestic markets, the nominal interest rate in local currency may be higher than the nominal interest rate in USD.
Moreover, in adverse Balance of Payment position, dollar loans will help to tide over the adverse situation.